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PROVINCIAL GOVERNMENT
REPUBLIC OF SOUTH AFRICA

PROVINCIAL TREASURY

Ref: 12/1/3/3/4/5

Enq: L S Mahaye

To: Municipal Manager
Thulamela Local Municipality
Private Bag X5066
THOHOYANDOU
0950

CC: Chief Financial Officer

**Subject: Feedback on 2016/2017 Adopted budget**

This letter serves to acknowledge receipt of the municipality's final budget for the 2016/17 financial year. Herewith please find this report which is a summary of findings and recommendation emanating from the review performed on the final budget.

You are advised to consider the contents of this report during the preparation of the 2016/17 adjustment budget.

In compliance with the Municipal Budget and Reporting Regulations, please advise the Mayor to table this report in council.

Yours in public finance management

**G PRATT (CA) SA**
**HEAD OF DEPARTMENT**

28/7/2016
**DATE**

Ismini Towers, 46 Hans Van Rensburg Street, POLOKWANE, 0700, Private Bag X9486, POLOKWANE, 0700
Tel: (015) 298 7000, Fax: (015) 295 7010 Website: http/www.limpopo.gov.za

LIMPOPO

PROVINCIAL GOVERNMENT

REPUBLIC OF SOUTH AFRICA

# PROVINCIAL TREASURY

THULAMELA LOCAL MUNICIPALITY

2016/17 FINANCIAL YEAR ADOPTED MTREF BUDGET ASSESSMENT REPORT

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## 1. Executive Summary

In terms of the requirements of the Municipal Finance Management Act and as part of its oversight role over local government finances. the Provincial Treasury is responsible for reviewing and commenting on the tabled budgets of all delegated municipalities prior to their adoption by the respective municipal councils The tabled budgets of these municipalities were rigorously assessed in terms of quality and compliance with the prescriptions of the MFMA and the Municipal Budget and Reporting Regulations.

## 2. Brief description of analyses process (techniques)

The analyses cover areas such as, amongst others:

- Compliance with legislative framework and the Regulations:
- Comparison of actual financial performance against budget (for both capital and operating budgets):
- Cash position of the municipality and its ability to fund budgeted expenditure;
- Medium Term Revenue and Expenditure Framework (MTREF) appropriations and their credibility, affordability and sustainability;
- Contribution of the budget to national and provincial government priorities:
- Responsive of the budget to the Integrated Development Plan (IDP);
- Proposed investments in infrastructure and impact on Local Economic Development and job creation;
- The rates and tariffs proposed; and
- Support of the budget to indigent households:

## 3. Linkage of the Strategic Risks to the IDP and MTREF Budget

The strategic risks register for 2016/17 has been submitted to the Provincial Treasury. Under Service delivery and Infrastructure development, the municipality indicated that lack of resources such as construction material and equipment has been delayed due to rain. In this case the municipality is managing the situation through intergovernmental structures.

The municipality indicated that new council might come up with new priorities and priorities and some of them will be coming to a local municipality for the first time. The municipality needs trainings and also SALGA induction workshop for new council. Furthermore. the municipality has identified poor revenue collection rate. The municipality has a credit control and debts collection policy which needs to be fully implemented to enhance revenue management.

The municipality is currently experiencing protests by communities for water, sanitation, and other services. The municipality do have controls in place to manage the situation. Lack of business continuity plan and Disaster recovery plan is partially implemented.

## 4. Procurement Plan

- The linkage between budget and the procurement plan is not verified due to non – submission of the procurement plan.

## 5. MFMA & MBRR Compliance

- Provincial Treasury has undertaken an assessment of the final budget that was adopted by the municipal council on the 27 May 2016 and submitted to the Provincial Treasury in both electronic and hard copy format on the 14 June 2016. The municipality's 2016/17 adopted budget has been prepared in the required format (i.e. 2.8 version) as stipulated in the Regulation 9 of the MBRR.

## 6. Draft comments consideration

| Summary of draft budget key observations | Consideration of Treasury inputs into the adopted budget |
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| **Revenue framework** | |
| • The municipality has increased the budget from R43.5 million to R56.6 million by 23.3 percent in the 2016/17 final budget. However, the municipality decreased the corresponding Debt impairment expense in Table A4, therefore, the surplus for the year is overstated. The municipality did not provide for the increase in the budget narrative report. | • Provincial Treasury's comment was not considered when the municipality finalised the 2016/17 Adopted Budget. |
| • The municipality has not budgeted for Cost of free basic services in Tables A4; SA1 and SA21. This appears unreasonable as the municipality provides free basic services to targeted households, for example, indigents. The | • The municipality did not consider Provincial Treasury's comments. |

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| indigent policy indicates that Council should at least take into consideration the extent of subsidisation of tariffs for poor households. Property rates and Service charges are overstated in Table A4 for the 2016/17 final budget. | |
| • Provincial Treasury is still unable to assess reasonableness of the budget for Interest earned – external investments, as the Final budget narrative report indicates that the calculation of interest earned is also based on all interest received from call accounts which are not reflected on the Table SA16. The municipality anticipated a decrease Call investment deposits in Table A6 for the 2016/17 final budget from R200 million to R100 million. Furthermore, the municipality has not considered neither any withdrawals nor any top ups in Table SA16 which appears inconsistent with the nature of some of the investments (Call investments deposits). Thus, Provincial Treasury is still unable to comment on the reasonableness of the budget for Interest earned- external investments. | • The reason provided by the municipality in the budget narrative report was not clear to substantiate the increase of R9 million or 28.1 percent on this line item in the 2016/17 final budget. |
| • In the final budget, the municipality has increased their budget for Fines from R9 million in the draft budget to R13 million in the final budget. In the final budget narrative | • In the budget narrative report, the municipality has substantiated the increase of Fines in the 2016/17 final budget. |

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| report, the municipality indicated that the increase includes traffic fines and illegal use of land fines. | |
| • Agency services have increased by R2.8 million or 18.9 percent from 2015/16 to 2016/17. The increase appears unreasonable in light of headline inflation rate of 6.6 percent as per the MFMA Circular 79 guideline. Furthermore, as per the Section 71 report for the month ending May 2016, the municipality did not raise any amount against the 2015/16 budget. | • During benchmarking exercise. Provincial Treasury requested the municipality to be realistic and consider the guidelines from the MFMA Circular 79 when preparing their 2016/17 final budget. |
| • The municipality still has not provided the breakdown for Other revenues of R70 million reflected in Table SA1. Provincial Treasury noted that the budget for Other revenue had increased by 74.7 percent from R17.7 million in 2015/16 to R70 million in the final budget. Although the final budget narrative report states that the revenue for Other revenue includes Selling of site, Tender document, building plans, clearance certificates and Hawkers licence. how, the municipality did not indicate how much is budgeted on these line items Provincial Treasury is unable to comment on the reasonableness of the budgeted revenue as the municipality has not provided any supporting documents | • Provincial Treasury's comments were partially attended, but no budgeted amount has been recorded under those items listed in the budget narrative. |

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| relating to the budgeted revenue of R70 million. | |
| **Expenditure Framework** | |
| • Provincial Treasury noted that Employee related costs were budgeted to increase from R202 million in 2015/16 to R223.8 million in 2016/17 which is 9.5 percent. The municipality has budgeted an amount R9.7 million for Senior managers in Table SA22, which does not reconcile to an amount of R9.4 million in Table SA23. Thus, Provincial Treasury is still unable to determine the reasonableness behind the budget of employee related costs. Furthermore, the municipality did not justify the increase in the budget document. | • In the Draft budget assessment, the municipality was advised not to exceed the average CPI of 6.6 percent plus 1 percent in the 2016/17 budget as per the guideline from MFMA circular 79. |
| • The municipality has decreased provision for Debt Impairment from R89.8 million in the 2015/16 financial year to R82 million in the 2016/17 final budget. In the budget document, the municipality stated that Provision for doubtful debts constitute 10 percent of the total budget due to non-payment of debts and contribution to provision for doubtful debts has be based on the current collection trend. As per the Section 71 monthly returns (Age Debtors) submitted by | • In the 2016/17 final budget, the municipality did not consider the comments from Provincial Treasury. As per the 2014/15 Audited AFS, the Age debtors increased from R344.9 million to R394.3 million for the period of month 11 in the 2015/16 financial year. |

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| the municipality to Provincial Treasury for month 11 (May 2016), it indicates that R346.3 million or 87.8 percent of total debtors of R394.3 million was outstanding for a period greater than 90 days. In light of the above, the municipality should consider providing for Debt impairment in the 2016/17 Adjustments budget. | |
| • A huge decrease of 15.9 percent from R234.6 million in 2015/16 to R203.3 million in 2016/17 was noted against Other expenditure with no explanation provided by the municipality. The budget for General expenses still constitutes 45.4 percent of total Other expenditure. No further disclosure was made in respect of this item. In light of the above, Provincial Treasury could not assess whether the municipality has budgeted for non-priority expenditure and determine the reasonableness thereof and compliance with MFMA Circular No. 58 and 66. | • Provincial Treasury's comment was not considered by the municipality when preparing the 2016/17 final budget. |
| • Based on the concerns raised above regarding overstatement of operating revenue and understatement of operating expenditure, the operating surplus of R62.6 million as budgeted in the 2016/17 final budget appears to be overstated. | • During benchmarking exercise, Provincial Treasury requested the municipality to be realistic when preparing their 2016/17 final budget. |

| Asset Management | |
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| • The municipality has not budgeted for Renewal of existing assets. This is not in line with MFMA Circular No. 66 which states that at least 40 percent of the capital budget must be allocated to Renewal of existing assets. In the budget narrative report, the municipality indicated that most of the new asset and renewal were done last three financial year. | • The municipality did not consider input from Provincial Treasury when preparing the 2016/17 final budget. |
| • MFMA Circular No. 66 states the municipality's Repairs and maintenance should not be less than 10 percent of the municipality's operating expenditure for municipalities that had a qualification on PPE values. The municipality has budgeted R19.4 million (3.2 percent) of the total operating expenditure of R612.8 million in 2016/17 as Repairs and maintenance. Furthermore, Repairs and maintenance has decreased by 56.5 percent from R30.4 million in the 2015/16 to R19.4 million in the 2016/17 budget. In the budget document, the municipality indicated that Repairs and maintenance are mainly done In house. Repairs and maintenance is below 8 percent and the municipality will be able to deal with all items that needs to be repaired or maintained in 2016/17 financial year. | • Provincial Treasury's comments were not considered by the municipality when preparing the 2016/17 final budget. As per MFMA Circular No. 58, if the budgeted amount for Repairs and maintenance reflected on Table A9 is less than 8 percent of the municipality's PPE asset value for the previous financial year, the municipality should provide a detailed explanation and assurance that the budgeted amount is adequate to secure the ongoing health of the municipality's infrastructure supported by reference to its Asset Management Plan. |

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| **Cash backed reserves/Accumulated surplus** | |
| • The municipality did not consider the inclusion of statutory requirements, Other provisions. Unspent conditional transfers and Reserves to be cash backed by cash/ investments in Table A8 | • Inputs from Provincial Treasury were not considered and the municipality did not provide the narrations in the budget document. |
| • Furthermore, the municipality has not fully populated Table A8 in respect of Long – term investments committed. | • Inputs from Provincial Treasury were not considered and the municipality did not provide the narrations in the budget document. |
| • Considering the concerns raised in the population of the final budget Tables A4, A5 and A7, the opening balance of R200 million appears highly questionable. | • Inputs from Provincial Treasury were not considered and the municipality did not provide the narrations in the budget document. |
| • Other current investments > 90 days of R277.9 million does not reconcile to Call investment deposits > 90 days in Table SA3, thus Provincial Treasury is unable to comment on the reasonableness of the budgeted amount. | • Inputs from Provincial Treasury were not considered and the municipality did not provide the narrations in the budget document. |
| • Considering all the concerns raised over the population of Tables A4 and A7 and the completeness of Table A8, the | • Inputs from Provincial Treasury were not considered and the municipality did not provide the narrations in the budget |

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| surplus of R610 million reflected in Table A8 is still highly questionable. | document. |
| **Cash flow** | |
| • The municipality's cash flow still contains errors as the adjusted budget columns do not reconcile with the 2015/16 Approved Adjustments budget. Therefore, incorrect balances were carried forward over the MTREF. | • During benchmarking exercise, the municipality was advised to use the correct source documents to complete information in the 2016/17 final budget. |
| • The municipality budgeted to receive cash inflows amounting to 36.64 percent of Property rates to be billed. The applied collection rate is questionable in relation to the collection rate of 40 percent reflected in the budget document. thus, cash inflows related to this revenue source is understated. | • Provincial Treasury's comments were not considered when preparing the 2016/17 final budget. The municipality did not apply the realistic collection rate as reflected in the budget documents. |
| • The Government – operating transfers in Table A7 of R398.5 million do not reconcile to the Government – operating transfers in Table A4 of R406.3 million. Therefore, the cash inflow in Table A7 is understated. | • The municipality did not consider inputs from Provincial Treasury when preparing the 2016/17 final budget. |

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| • Furthermore, Government – capital in Table A7 of R94.7 million does not reconcile with Transfers recognised – capital in Table A4 of R110.7 million. Therefore, the Government – capital in Table A7 is understated. | • Provincial Treasury's inputs were not considered when preparing the 2016/17 final budget. |
| • While the municipality has budgeted for opening Cash and cash equivalents balance, the basis of calculation was not provided in the final budget narrative report nor was the calculation populated in the full year forecast column, thus, Provincial Treasury is unable to comment of the reasonableness thereof. | • The municipality was advised to be prudent when anticipating the Opening balance in Table A7. |
| • There is no correlation of amounts in Table A7 of R205.6 million for Cash and cash equivalents for 2016/17 and Table A6 of R483.5 million for Cash plus Call investments less Bank overdraft. | • Provincial Treasury's inputs were not considered when the municipality prepared the 2016/17 final budget |

## 7. Credibility (Funding), Relevance and sustainability of the final budget

This section aims to assess the credibility (funding), Relevance and sustainability of the adopted budget. Reference is made to your approved budget for the 2016/17 financial year that was submitted to Provincial Treasury in accordance with Section 24(3) of the Municipal Finance Management Act (MFMA), which states that the accounting officer of a municipality must submit the approved annual budget to the National Treasury and relevant Provincial Treasury.

Provincial Treasury has conducted a high level assessment of your approved budget with a view of assessing whether the municipality has considered the comments and recommendations provided by Provincial Treasury on your tabled budget, as required by Section 23(1)(b) of the MFMA. Section 23(1)(b) states that the municipal Council must consider any views of the National Treasury, the relevant Provincial Treasury and any provincial or national organs of state or municipalities which made submissions on the budget

**Credibility**

There were minor discrepancies noted in the audited outcomes and Adjustments Budget figures completed in the A Schedules in comparison to the Audited Annual Financial Statements (AFS) and the adopted 2015/16 Adjustments Budget.

Provincial Treasury's assessment was limited to a large extent due to the budget assumptions and basis of calculation being unclear and in many instances questionable.

As per the Cash Flow Statement Tables A7 and Cash backed reserved/ accumulated surplus reconciliation Table A8, the municipality's 2016/17 final budget is funded. However, the municipality is requested to rectify all errors identified by Provincial Treasury relating to the budgeted cash flow statement in order for Provincial Treasury to determine the municipality's true finding position. The municipality is advised to manage the associated risks of implementing the budget, and ensure that spending is limited to what can be realistically collected in revenue, as required by Section 18 of the MFMA. Furthermore, the municipality will

be required to consider all comments from Provincial Treasury during the 2016/17 Adjustments budget process.

**Relevance**

Total revenue budget for IDP strategic objectives in Table SA4 (R728.9 million) does not reconcile with the Total revenue in Table A4 (R675.4 million) in the final budget. Thus, the IDP strategic objectives relating to operating revenue in are not aligned to the final budget.

**Sustainability**

Revenue and expenditure management is fundamental to the sustainability of the municipality. The municipality has budgeted for an operating surplus over the MTREF. The municipality's operating budget continues to be mainly funded from grants by 60.1 percent.

The municipality is encouraged to investigate other sources of revenue in order to decrease their grant dependency and at the same time ensure that their current revenue stream is adequately managed.

## 8. Conclusion

The municipality complied with the requirements of MBRR. The municipality should address the inconsistencies that are indicated in the 2016/17 final budget and ensure that they are corrected during the 2016/17 Adjustments budget.

## 9. Recommendations

The municipality is advised to manage the associated risks of implementing the budget, and ensure that spending is limited to what can be realistically collected in revenue, as required by Section 18 of the MFMA.

In terms of MFMA Circular No. 67, the municipalities are reminded to upload all their 2016/17 related annual budget returns to National Treasury's local government database before the end

of July 2016. As National Treasury publishes the municipal budgets based on the information from annual budget returns, the municipalities are therefore, required to ensure that the figures reflected in the annual budget returns correspond with the figures as per the approved budget (Schedule A1 Version 2.8).

Prepared by:

21/07/2016

Mahaye L S
Deputy Director: Financial Planning and Budget

Date

Reviewed by:

25/07/2016

Mbungela N N
Director: Accounting and Reporting

Date